

CITY OF SAN JOSÉ

Item 3.4 Retirement Reform: 2nd Tier Benefits

January 25, 2011

Retirement Information

www.sanjoseca.gov

- Click on **City Departments** (left column)
- Click on **Employee Relations** (Under City Manager's Office)
- Click on **Retirement Benefits Information**

<http://www.sanjoseca.gov/employeeRelations/RetirementBenefits.asp>

Agenda

- Council Direction
- Retirement Reform
- Why is a 2nd Tier Needed?
- Overview of Current San Jose Retirement Benefits
 - What They Cost and Who Pays
- 2nd Tier Retirement Benefit Options
- Recommendations
- Status of Negotiations

Council Direction – November 18th

- Direct staff to continue analysis of options for a 2nd Tier retirement program and return to Council with recommendations in early 2011
- Options should include:
 - Input from the General Fund Structural Deficit Elimination Plan (GFSDEP) Stakeholder Group
 - The City Auditor's recommendations

Retirement Reform

Primary Retirement Reform Categories

1. Keeping up with funding requirements
2. Improving governance and investment oversight
3. Reducing benefits or increasing the retirement age
4. Sharing the risk with employees
5. Increasing employee contributions

*-The Pew Center on the States: The Trillion Dollar Gap-
Underfunded State Retirement Systems and the Road to Reform*

Why is a 2nd Tier Needed?

“[I]t is important that the City move aggressively to rein in pension costs that threaten the stability of the General Fund and the services it provides to the residents of San Jose.”

- Pension Sustainability Audit Report
City Auditor's Office

“There is widespread concern that the cost of employee total compensation continues to increase while revenues and services decrease.... Pension and health care benefits have risen substantially since 2000.... The overall costs to cities are not sustainable. Cities need to negotiate, approve and implement considerable cost containment measures so that employee financial obligations do not continue to escalate.”

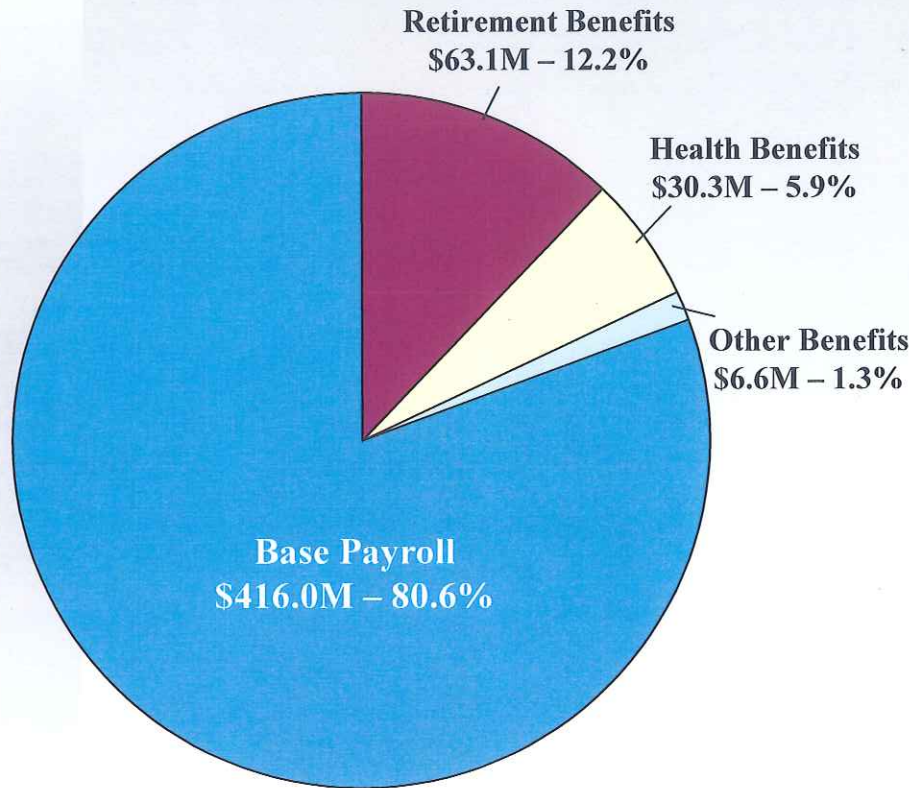
- Cities Must Rein In Unsustainable Employee Costs
Santa Clara County Civil Grand Jury

10-Year Growth in Total Compensation

Fiscal Year 2000-2001

\$516 Million

7013 FTEs

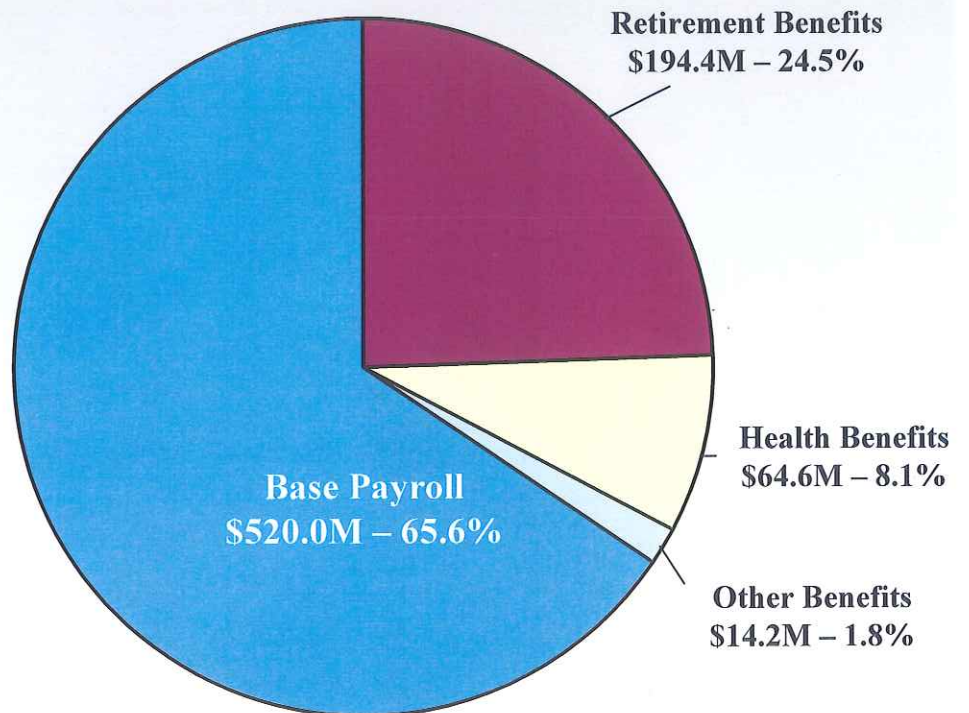


Source: Salary and Fringe Benefit Costs by Bargaining Unit & Fund for the 2000-2001 Adopted Budget

Fiscal Year 2011-2012

\$793 Million

5669 FTEs



Source: Salary and Fringe Benefit Costs by Bargaining Unit & Fund for the 2011-2012 Base Budget

Overview of Current San Jose Retirement Benefits

Pension Benefits Summary

	Federated	Police/Fire
Minimum Age	55 Any age with 30 years of service	50 Any age with 30 years of service
Maximum Benefit (at 30 years of service)	75%	90%
Annual Cost of Living Adjustment (COLA)	3% Fixed (compounded)	3% Fixed (compounded)

Average Annual Pension

2006-2010 ¹		
	Total Pension ²	Average Years of Service
Federated	\$43,729	20.22
Police and Fire	\$100,202	26.32

Note:

¹ Includes approved retirements through October 31, 2010

² Does not include the value of Retiree Healthcare Benefits

Federated Total Pension includes people who only work for City for 5 years

Other Pension Benefits

- Survivorship Benefits
- Supplemental Retiree Benefit Reserve (SRBR) (“13th Check”)
- Reciprocity
- Disability Retirements
- No offset for Workers’ Compensation benefits received (Police and Fire Only)

Current Retiree Healthcare Benefits

	Federated	Police and Fire
Maximum Benefit	100% of Lowest Priced Plan for Single or Family	100% of Lowest Priced Plan for Single or Family
Eligibility	Medical: 15 years of service Dental: 5 years of service	Medical and Dental: 15 years of service or 20 years for those who leave prior to retirement

Kaiser	Single Coverage (Annual)	Family Coverage (Annual)
2011	\$5,952	\$14,822

Current Benefits:

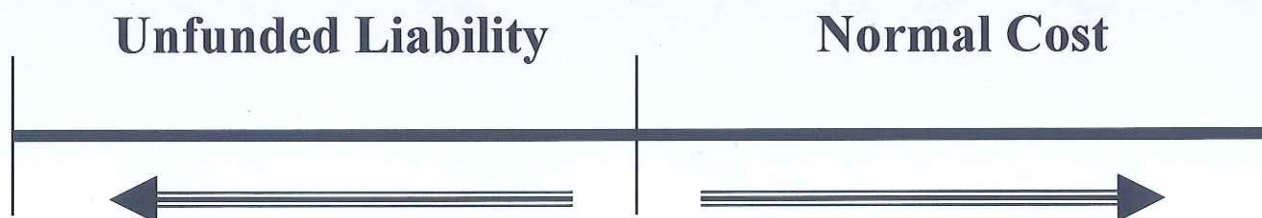
What They Cost and Who Pays

The actuarial assumptions do not determine the “actual cost” of the plan. The actual cost is determined solely by the benefits and administrative expenses paid out, offset by investment income received. However, it is desirable to estimate as closely as possible what the actual cost will be so as to permit an orderly method for setting aside contributions today to provide benefits in the future, and to maintain equity among generations of participants and taxpayers.

- The Segal Company report dated November 22, 2010

Retirement Contribution Rates

$$\text{Total Contribution} = \text{Normal Cost} + \text{Unfunded Liability Amortization}$$

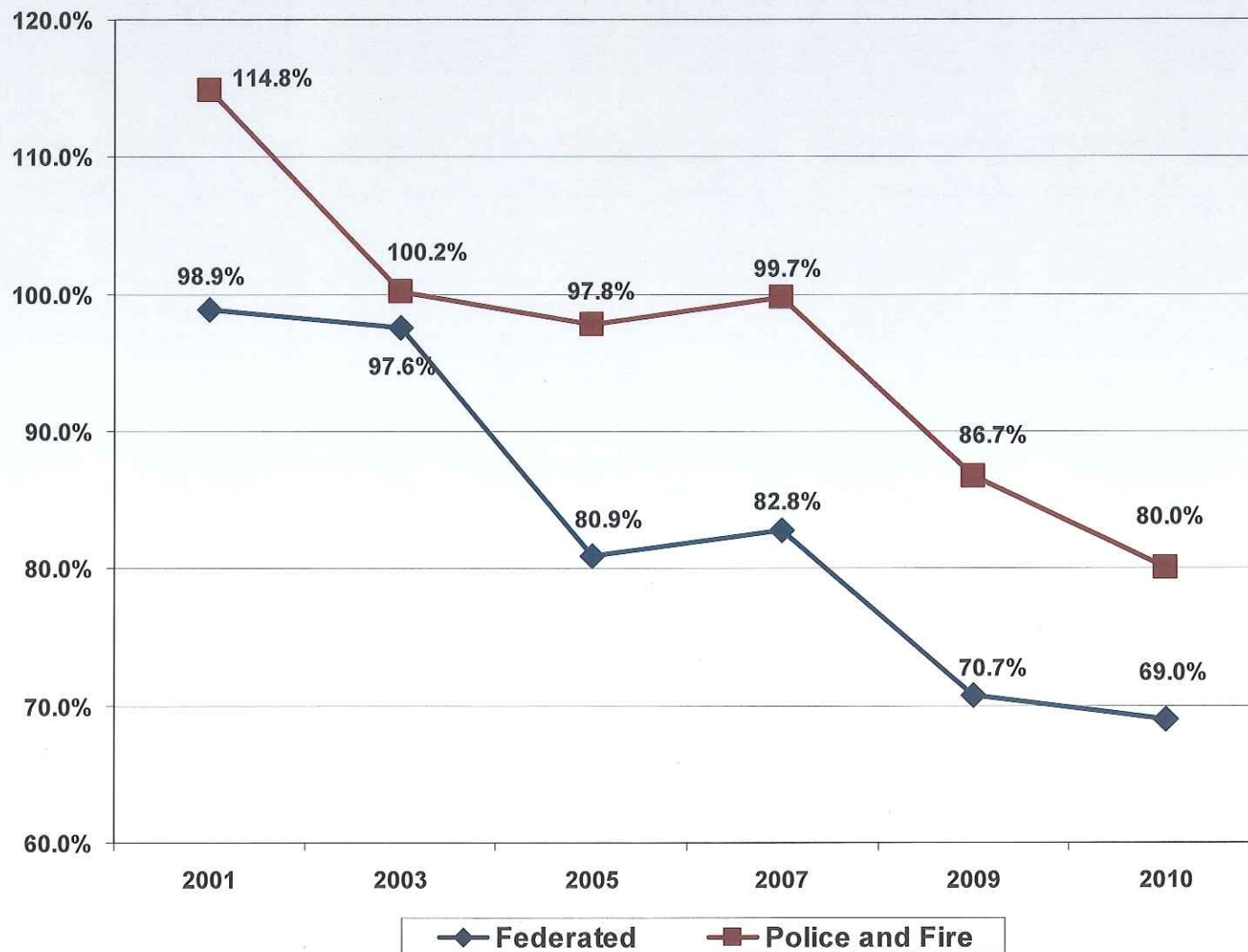


Unfunded Liability

	Federated	Police & Fire	Total
Actuarial Value: Unfunded Accrued Actuarial Liability	\$1.6B	\$1.36B	\$2.96B
Market Value: Unfunded Accrued Actuarial Liability	\$1.82B	\$1.72B	\$3.54B

Source: Valuation Date: June 30, 2010 (with exception of Police and Fire Retiree Healthcare – June 30, 2009 Valuation)

Pension Funding Ratios (Actuarial Value)



Funding Ratios – June 30, 2010

Retirement Funding Ratios As of June 30, 2010		
Pension	Federated	Police and Fire
Market Value	60%	69%
Actuarial Value	69%	80%

Retiree Healthcare (OPEB) Plans	Federated	Police and Fire
Market Value	12%	7%
Actuarial Value	12%	6%

Key Factors That Impact Retirement Costs

- Benefit Levels/Enhancements
 - Pension Formula
 - Cost of Living Adjustment (COLA)
 - Final Average Salary
 - Retirement Age
 - Retiree Healthcare

Fiscal Year 2011-2012 City Costs

	Pension	Retiree Healthcare
Total for All Funds	\$208.7 M	\$39.0 M
Grand Total for FY 11-12	\$247.7 M	

Note: Includes City's pre-payment discount

Fiscal Years 10-11 & 11-12 Retirement Contribution Rates

Federated City Employees' Retirement System				
	City		Employee	
	FY 10-11	FY 11-12	FY 10-11	FY 11-12
Pension	23.18%	28.34%	4.54%	4.68%
Medical and Dental	6.41%	7.16%	5.76%	6.51%
Total	29.59%	35.50%	10.30%	11.19%
Police and Fire Department Retirement Plan (Police)				
	City		Employee	
	FY 10-11	FY 11-12	FY 10-11	FY 11-12
Pension	38.32%	49.78%	9.81%	10.46%
Medical and Dental	6.26%	6.26%	5.76%	5.76%
Total	44.58%	56.04%	15.57%	16.22%
Police and Fire Department Retirement Plan (Fire)				
	City		Employee	
	FY 10-11	FY 11-12	FY 10-11	FY 11-12
Pension	40.24%	51.54%	10.09%	10.76%
Medical and Dental	3.92%	3.92%	3.61%	3.61%
Total	44.16%	55.46%	13.70%	14.37%

Does not include City's pre-payment discount

5 unions paying a % of City's UAAL

Police and Fire Medical and Dental rates for the City and employees are for FY 10-11. It is anticipated that the FY 11-12 rates will be available in February.

Rising Retirement Costs Account for Over Half of 2011-2012 General Fund Budget Shortfall

	2011-2012 PRELIMINARY FORECAST SHORTFALL	2011-2012 UPDATED FORECAST-RETIREMENT*
Carry-Over from 2010-2011 Adopted Budget	\$ 20.5 M	\$ 20.5 M
Increased Retirement Contribution Rates*	21.5 M	60.9 M
Increased Health Care Costs	4.1 M	4.1 M
Salary Step/Performance Increases	3.1 M	3.1 M
2011-2012 Committed Additions	6.6 M	6.6 M
Public Safety Vehicle Replacement	4.4 M	4.4 M
Other Expenditure Adjustments	0.2 M	0.2 M
Decreased Revenue Estimates	9.5 M	9.5 M
TOTAL 2011-2012 GENERAL FUND SHORTFALL	\$ 69.9 M	\$ 109.3 M

* Updated Retirement Contribution information only, updated 2012-2016 Forecast to be issued in late February; Increased Retirement Contributions: Police (\$26.7 M), Fire (\$18.7 M), Federated (\$15.5 M); Does not include updated Police & Fire retiree healthcare changes.

Projected City Retirement Contributions Exceed \$1.7 Billion Over Next Five Years (All Funds)

Retirement Plan	FY 11-12	FY 12-13	FY 13-14	FY 14-15	FY 15-16
Federated	\$112.6M	\$133.6M	\$158.6M	\$171.2M	\$176.2M
Police	\$89.7M	\$110.6M	\$126.1M	\$136.2M	\$140.4M
Fire	\$53.9M	\$66.3M	\$75.5M	\$81.5M	\$84.1M
TOTAL	\$256.2M	\$310.5M	\$360.2M	\$388.9M	\$400.7M
% Increase		21.19%	16.01%	7.97%	3.03%

2nd Tier Retirement Benefits for New Employees

City Charter Amendment

- November 2nd Passage of Measure W
- Allows for adoption of an ordinance to exclude future City officers and employees from any existing retirement plans or benefits
- Allows City to establish retirement plans for future employees that do not provide for the current minimum requirements and cost sharing

City Auditor Recommendations

- Pursue one or a combination of pension cost-containment strategies:
 - Additional cost sharing
 - Eliminating or limiting SRBR transfers/distributions
 - Negotiate prospective changes for existing employees
 - Establish a 2nd tier for new employees
 - Consider joining CalPERS to reduce administrative costs

General Fund Structural Deficit Elimination Plan Stakeholder Group

- Top 5 high-level ideas for potential changes
 - Create a 2nd Tier pension system for new employees
 - Increase the retirement age
 - Change automatic 3% COLA to link increases to CPI or to increase given to Social Security
 - Change to a defined contribution plan or hybrid
 - No City Pension holiday; always pay full normal cost

Goals of 2nd Tier Retirement Benefits

- Minimize intergenerational transfers of the cost of retirement benefits
 - Unavoidable given the current unfunded liability
- Long-term sustainable benefits
- Reduce future costs
- Reduce risk

Competitiveness

- Can't use model that relies primarily on comparisons of retirement benefits of other cities
 - State started 90% benefit for public safety
 - Spread throughout California
 - Competitiveness was main reason given for need to provide a 90% retirement benefit

Competitiveness

“Designing a retirement plan that attracts and retains all workers is not possible because of lifestyle differences. This is further complicated by the age differences of new employees and their life priorities. Increased job marketplace mobility means that workers of all ages enter employment at different stages of their careers and stay for differing lengths of time. What attracts older workers may be very different from what attracts younger workers. Further, what attracts younger workers today may provide a source of regret as they age and wish they had chosen differently.”

-Maine Unified Retirement Task Force Study and Report, March 2010

Competitiveness

- Primary consideration should be to fiscal health of the City and the City's ability to provide basic City services to residents
- Recruit employees who are interested in a career in public service
- San Jose is a major employer
 - More employees than every city in Santa Clara County (combined)
 - San Jose can drive the market

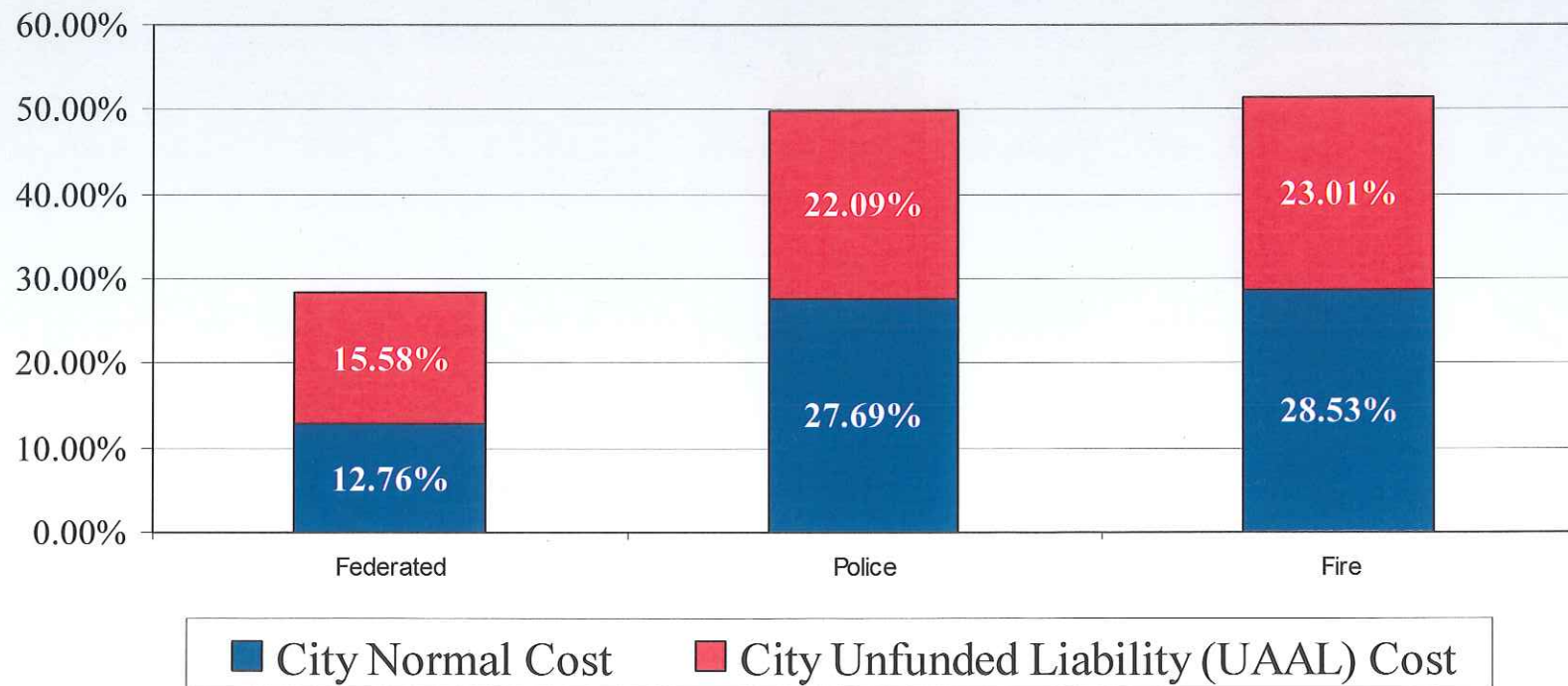
Goals of 2nd Tier Retirement Benefits

- A cost and structure of retirement benefits that provides for future flexibility
 - Allows for total compensation dollars to be directed at pay or other benefits in the future
 - Allows for flexibility to react to the labor market

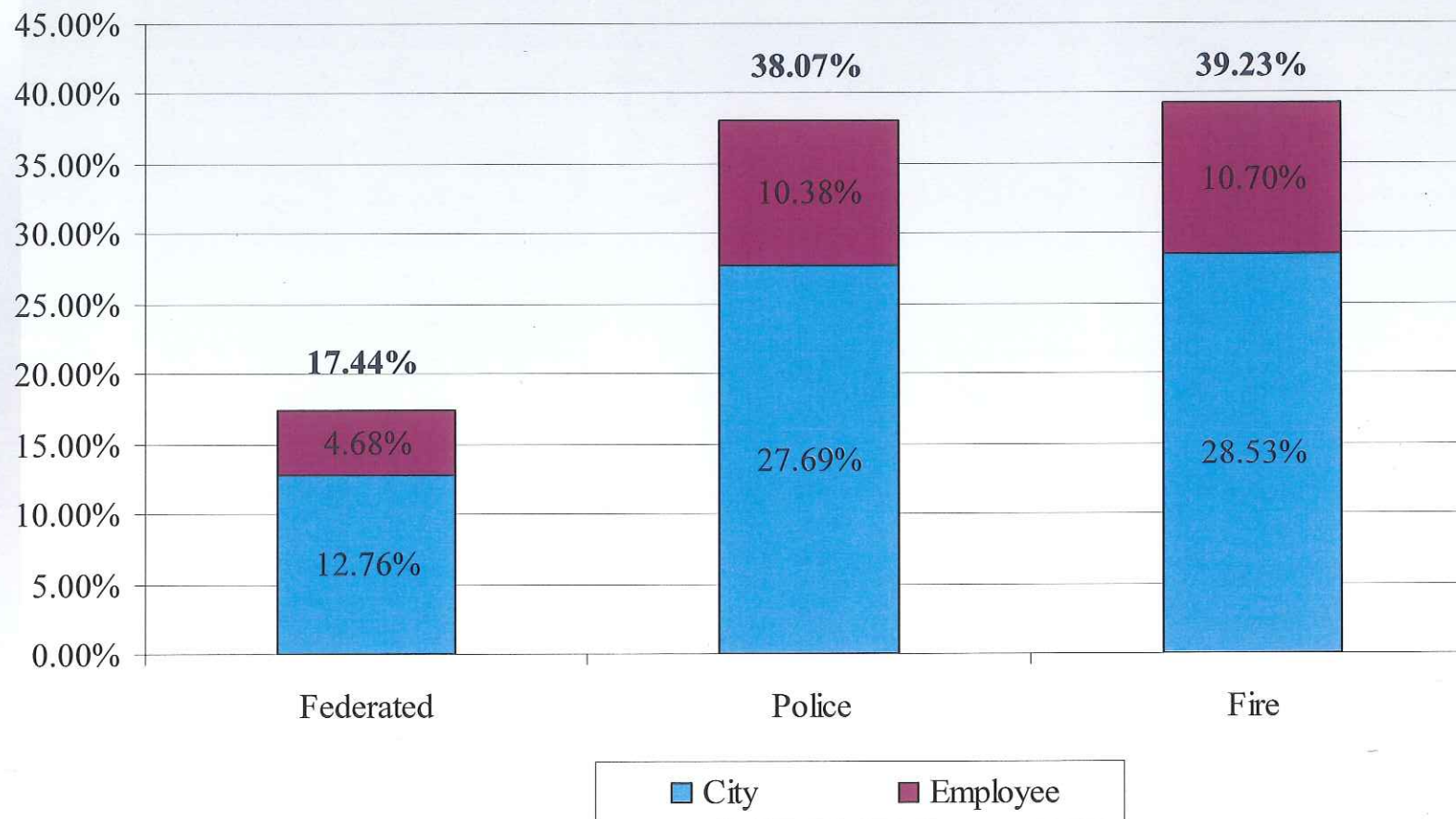
Alternatives for a 2nd Tier

- Defined Benefit Plan
- Defined Contribution Plan
- Social Security
- Hybrid

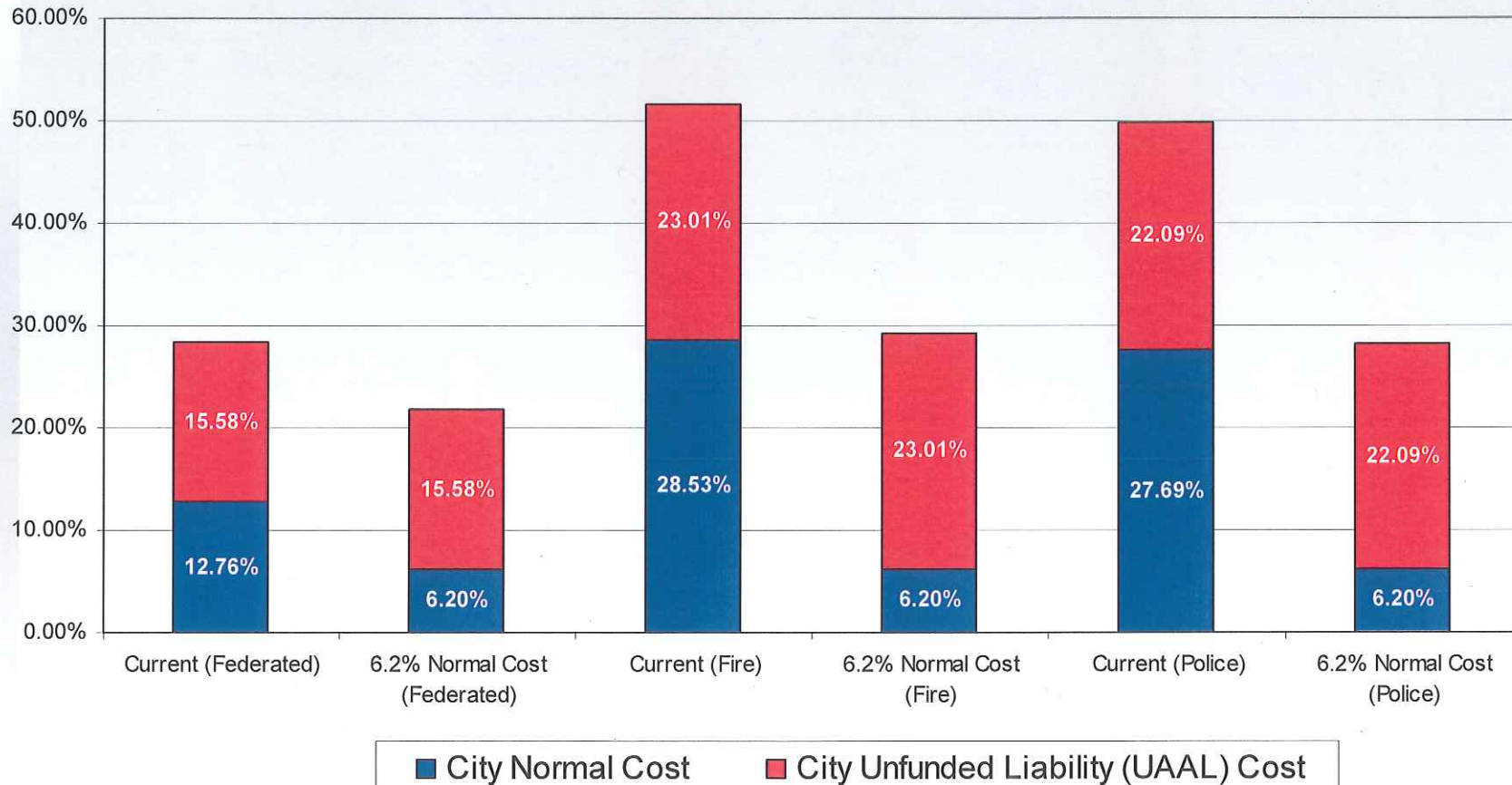
City's FY 11-12 Pension Costs – Normal & Unfunded Liability



FY 11-12 Pension Normal Cost – City and Employees



Current City Pension Costs compared to 6.2% Normal Cost (12.4% Total)



Alternative Defined Benefit Plan Designs: Maximum 12.4% Normal Cost

Alternative Pension Benefit	
Formula	1.25% – 2.00% per year of service
Age	58 – 65
COLA	0 – 2%
Calculation of Pension	Modify from current highest final year

Estimated Future Annual Savings

Assumes City's Normal Cost is 6.2%

New Hires	Savings
33% in 5 Years	\$21.9 M
50% in 10 Years	\$33.1 M

Note:

Assumes FY 11-12 Base Budget for estimated savings as of October 2010 Base Budget.

Assumes rates that have been approved by the retirement boards to date.

Assumes that FY 11-12 rates would remain unchanged for the next 10 years.

**2nd Tier Retirement Benefits
for
New Employees
Recommendation/Direction**

Recommendations for 2nd Tier Retirement Benefits for New Employees

- 2nd Tier Normal Cost not to exceed 6.2% for the City
 - Defined Benefit or Hybrid Plan
- Considerations for Defined Benefit
 - Cost Sharing – Pension Unfunded Liability
 - Cost of Living Adjustment (COLA)
 - Retirement Age
 - Pension Formula
 - Determination of Final Compensation
 - Retirement Service Credit

Recommendations for 2nd Tier Retirement Benefits for New Employees

- Considerations for Defined Benefit (cont'd)
 - Minimum Service Requirements (Vesting)
 - Joint and Survivor Benefits
 - Retiree Healthcare Benefit
 - Cost Sharing – Retiree Healthcare
 - Retiree Dental Benefit
 - Retroactive Disability Retirement Applications

Other Retirement Reforms

- Options for current employees
- Supplemental Retiree Benefit Reserve (SRBR) (“13th Check”)
- Workers’ Compensation Offset in the Police and Fire Department Retirement Plan

Status of Retirement Benefits Negotiations

Bargaining Unit	Negotiation Start Date
POA	January 12, 2011
MEF	January 19, 2011
CEO	January 19, 2011
ABMEI	January 21, 2011
IBEW	January 21, 2011
AEA	January 21, 2011
CAMP	January 21, 2011
AMSP	January 21, 2011
ALP	January 24, 2011
OE#3	February 2, 2011
IAFF	N/A

Questions and Discussion